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UNCLAS SECTION 01 OF 02 ASUNCION 000926

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STATE PASS TO USTR FOR LYANG
USAID FOR AA/LAC ADOLFO FRANCO
TREASURY FOR OSIA MAUREEN WAFER
COMMERCE ITA SARAH COOK
NSC FOR MIKE DEMPSEY AND SUE CRONIN
SOUTHCOM FOR POLAD
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E.O. 12958: N/A

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SUBJECT: Putting It Together: Paraguay's Maquilas Provide
Open Door to MERCOSUR

REF: ASUNCION 714

Summary

¶11. In operation since 2001, Paraguay's maquilas are designed to stimulate local manufacturing for export. Under preferences unique to Paraguay, only forty percent of the content of the products must originate within MERCOSUR for the products to enter other MERCOSUR countries tariff-free. The sector is currently experiencing rapid growth. With 23 maquilas currently in operation, Paraguay hopes to expand the sector through marketing and promotion efforts. The GOP has included support to the maquila unit in its proposed country plan for the Millennium Challenge Account Threshold Program as a way to foster greater access to jobs in the formal sector, particularly in the tri-border region. End Summary.

Putting It Together

¶12. Paraguay's maquilas date to a series of investment strategies approved in 2001. Like other regimes in Mexico and Central America, the Paraguayan model is designed to stimulate local manufacturing, and provides for a local company to produce goods by adding value to foreign-produced inputs imported solely for the manufacturing process. The final product is then exported for final sale, though Paraguayan regulations do allow for limited local distribution.

¶13. The Paraguayan maquila regulations allow for both the traditional industrial production and the provision of services. Regulations provide for the input of tangible and intangible inputs which must be returned abroad by either tangible or intangible means, e.g. software or database information.

Grading For Content

¶14. The Ministry of Industry and Commerce's Rolando Diaz told Econ Chief that Paraguay's geographic location allows easy overland and/or river access to major South American markets in Argentina and Brazil, but that its true advantages for maquila operators lie in special product content preferences within the MERCOSUR trade area. Under an arrangement unique to Paraguay, only 40 percent of the inputs in Paraguay's maquila-produced goods must originate in the MERCOSUR area for the final products to enter the common market tariff-free. Inputs in this instance can include water, power, transportation, financing and labor, and may be sourced from any MERCOSUR member.

¶15. Paraguay's other advantages include competitive labor and energy costs, cheap land and a favorable tax structure for maquila goods. Producers are only required to pay one percent of the value added in Paraguay. They also enjoy a tax exemption on their investments, and are entitled to tax rebates on some costs such as electricity. Despite generous incentives to locate maquilas in the country, disadvantages to Paraguay-based production remain. While the day-to-day cost of labor in the country remains among the lowest in the region, there remains a lack of flexibility in labor regulations, meaning that employers can bear high costs if they must dismiss workers later. Paraguay's MERCOSUR preferences, designed to jump-start local manufacturing, will begin to phase out in 2008, reaching full parity with fellow member states in 2015.

Impressive Numbers

16. In spite of the generous incentives given to manufacturers under the 2001 maquila regulations, Paraguay's maquila sector has only recently seen large-scale growth. There are currently 23 maquilas in operation, with another 26 approved to begin production. Numbers released by the Ministry of Industry and Commerce (MIC) show that as of May 2005, maquila-produced exports totaled USD \$7,154,138, an increase of 137% over the same period in 2004. Among the leaders in maquila-produced exports are wood moldings and parquet flooring, tanned leather and swimwear.

17. As reported reftel, Brazilian company Mega Plasticos is investing USD \$18 million in a synthetic rubber factory under the maquila regime. Paraguay Vende, a USAID-sponsored initiative designed to facilitate legal commerce, provided Mega Plasticos with legal and other assistance that helped secure the company's decision to invest in Paraguay. Diaz told Econ Chief that the MIC is interested in promoting Paraguay's maquilas abroad, including to U.S. companies interested in entering the South American market. The GOP has included support to the maquila unit in its proposed country plan for the Millennium Challenge Account Threshold Program as a way to foster greater access to jobs in the formal sector, particularly in the tri-border region.

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